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Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

In the Matter of

Computer III Further Remand  
Proceedings: Bell Operating Company  
Provision of Enhanced Services

CC Docket No. 95-20

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REPLY COMMENTS OF MCI TELECOMMUNICATIONS CORPORATION

MCI TELECOMMUNICATIONS CORPORATION

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**Introduction and Summary**

MCI Telecommunications Corporation (MCI), by its undersigned attorneys, submits the following reply to the initial comments filed in this proceeding in response to the Notice of Proposed Rulemaking (Notice).<sup>1/</sup> In spite of the Bell Operating Companies' (BOCs') emphasis on the alleged benefits of joint provision of BOC basic and enhanced services, their presentations confirm MCI's view that structural integration has provided, and will provide, no significant benefits to the public, whatever financial benefits there may be for the BOCs. When this lack of benefits is balanced against the continuing abuses discussed in MCI's and other parties' initial comments and ex parte filings, it is even clearer than it was the last time around -- during the Computer III Remand proceeding<sup>2/</sup> -- that full structural separation must be maintained.

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<sup>1/</sup> FCC 95-48 (released February 21, 1995).

<sup>2/</sup> Report and Order, Computer III Remand Proceedings: Bell Operating Company Safeguards and Tier 1 Local Exchange Company Safeguards, 6 FCC Rcd 7571 (1991) (Computer III Remand Order), partly vacated sub nom. California v. FCC, 39 F.3d 919 (9th Cir. 1994).

The most striking aspect of the BOCs' initial comments is their similarity to the BOCs' comments in the Computer III Remand proceeding. The BOCs have little new to say concerning the supposed benefits of joint BOC basic and enhanced services, in spite of the intervening years of experience in providing such services. As MCI and other parties predicted, most of the BOCs' enhanced service growth has been in voice messaging. The BOCs' showing of cost savings from joint provision of services are, for the most part, about as shallow as they were in the past, which is quite surprising, given all of the additional time they have had to conduct more serious analyses. Once again, their showings of benefits from joint services are also undercut by their reliance on the unstated and unwarranted assumption underlying their presentations on this issue -- namely, that they are the only possible sources of certain categories of enhanced services.

The BOCs' comments concerning the risks of anticonsumer and anticompetitive conduct are similarly undeveloped since the Computer III Remand proceeding. Faced with the holdings of the Ninth Circuit in California II<sup>3/</sup> and California III<sup>4/</sup> as to the inadequacy of Open Network Architecture (ONA), the BOCs have retreated to the fallback position that the combination of ONA and the other antidiscrimination rules, together with other unbundling initiatives, are sufficient to prevent unlawful

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<sup>3/</sup> California v. FCC, 4 F.3d 1505 (9th Cir. 1993).

<sup>4/</sup> California v. FCC, 39 F.3d 919 (9th Cir. 1994).

discrimination. ONA, once the "centerpiece" of the Commission's antidiscrimination safeguards,<sup>5/</sup> has been pushed to the side. None of the BOCs explains how "ONA-lite" and the other antidiscrimination rules are going to prevent the types of abuses reflected in the previous and current records.

The BOCs once again also contend that their stranglehold over local network access has been sufficiently loosened by several factors, including local access competition, that they are no longer in a position to discriminate unreasonably. Upon closer inspection, this argument is also as weak as it was the last time around. The BOCs also repeat the usual litany of cost accounting rules and related protections against cross subsidies, ignoring the evidence of their ineffectiveness as revealed in recent federal and state audits. The BOCs thus have not borne their burden of demonstrating that there is now a sufficient basis for eliminating the structural separation requirement.

I. THE BOCs HAVE FAILED TO DEMONSTRATE SIGNIFICANT PUBLIC BENEFITS RESULTING FROM STRUCTURAL INTEGRATION

A. The BOCs' Presentations Are Based on a False Reading of History

The BOCs' presentations of the alleged benefits of structural integration are based on an elaborate myth only

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<sup>5/</sup> Brief for Federal Communications Commission at 26, California v. FCC, No. 87-7230 (9th Cir., filed May 27, 1988) (FCC California I Br.).

loosely related to recent developments in the enhanced services market. In the BOC myth, structural integration has led to a vast expansion of enhanced services by all providers, BOCs, local exchange carriers (LECs) and independent enhanced service providers (ESPs). Under that scenario, the vigorous BOC participation in the enhanced services market made possible by structural integration has spurred other providers to improve service and reduce rates. Other providers, who are allowed to offer all of their services on a joint basis, not only have not been injured by BOC unseparated enhanced services, but they also have even been improved by the BOCs' more vigorous competition, according to the BOCs.<sup>6/</sup>

The BOC discussions of this point all reflect the post hoc ergo propter hoc fallacy. The growth of non-BOC enhanced services in recent years has nothing to do with the BOCs' offering of unseparated enhanced services. Such growth was occurring when the BOCs were subject to structural separation and would have continued irrespective of how the BOCs' enhanced services were organized.<sup>7/</sup> As the BOCs concede, they have not become significant factors in most enhanced service markets or in

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<sup>6/</sup> See, e.g., Pacific Bell Comments at 1-4, 16-18, 74; US West Comments at 5, 11-13; Bell Atlantic Comments at 4-10.

<sup>7/</sup> Southwestern Bell, at 31, seems to acknowledge that the BOCs could not have been responsible for the growth in those enhanced service markets in which the BOCs have not become significant factors.

enhanced services overall,<sup>8/</sup> so it is impossible to ascribe significant public benefits to their participation or to the manner in which they have offered enhanced services in recent years.

The centerpiece of the BOC public benefits myth is the voice messaging experience. As was the case in the Computer III Remand proceeding, voice messaging continues to be the BOCs' only significant enhanced service,<sup>9/</sup> and they overwhelmingly dominate the "mass market" residential segment of the network-based voice messaging market.<sup>10/</sup>

As background to the recent developments in the voice messaging market, most of the BOCs recount the story of the Custom Calling Denial Order,<sup>11/</sup> without realizing its true

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<sup>8/</sup> BellSouth Comments at 56-57; US West Comments at 12; Ameritech Comments at 8; Bell Atlantic Comments at 5 n.6; Southwestern Bell Comments at 7-9, 15.

<sup>9/</sup> See Southwestern Bell Comments at 8-9; NYNEX Comments at 28; Pacific Bell Comments at 8; US West Comments at 10; Bell Atlantic at 5 n.6.

<sup>10/</sup> See Booz Allen & Hamilton Inc., The Benefits of RBOC Participation in the Enhanced Services Market at III-4 through III-6 (April 4, 1995), attached to US West Comments (graph shows LECs and BOCs account for over 85% of residential market); Declaration of Robert N. Garner at ¶ 4, attached to Bell Atlantic Comments (no competition for Bell Atlantic's voice messaging service other than answering machines). See also US West Comments at 12; Pacific Bell Comments at 15-17.

<sup>11/</sup> American Telephone & Telegraph Company Petition for Waiver of Section 64.702 of the Commission's Rules and Regulations, 88 FCC 2d 1 (1981).

lessons for this issue. In the BOCs' retelling, the Commission refused in that case to allow the unseparated provision of Custom Calling voice messaging service by the pre-divestiture AT&T, assuming that if AT&T chose not to provide voice messaging under structural separation, others would. Other providers did not come along, leaving the low end residential market unserved. Since the BOCs started providing unseparated voice messaging services, the residential voice messaging market has increased tremendously. The BOCs' conclusion is that the structural separation requirement deprived the public of voice messaging service.<sup>12/</sup> Six of the BOCs have submitted a report by Jerry A. Hausman and Timothy J. Tardiff (Hausman/Tardiff Report) purporting to show that the delay in introducing voice messaging service, resulting from the structural separation requirement, imposed a consumer welfare loss of nearly \$6 billion.<sup>13/</sup> The Commission drew a similar conclusion in the Computer III Remand Order.<sup>14/</sup>

Such an interpretation, however, is only possible by deliberately ignoring the most important aspects of the Custom Calling Denial Order. The Commission only assumed in that case

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<sup>12/</sup> BellSouth Comments at 52-54; Pacific Bell Comments at 3; Bell Atlantic Comments at 16; Southwestern Bell Comments at 30-31.

<sup>13/</sup> J.A. Hausman and T.J. Tardiff, Benefits and Costs of Vertical Integration of Basic and Enhanced Telecommunications Services at 14-15 (April 6, 1995).

<sup>14/</sup> 6 FCC Rcd. at 7618-19, ¶ 101.



that structural separation "does not necessarily foreclose the availability of similar services to consumers," 88 FCC 2d at 26, because other providers of voice messaging services would come along "if the local telephone companies provide the requisite interconnection facilities" needed by those other providers. Id. at 31 (emphasis added).

That is a big "if." In the Notice of Proposed Rulemaking in Computer III, the Commission noted that other voice messaging providers had not come along after the Custom Calling Denial Order and then stated:

Of course, the type of interconnection that might have been used by others to configure services of this nature, at costs comparable to those inherent in AT&T's proposed custom calling services, was unavailable.... Had comparably efficient interconnection been available, other might be providing such services today. Absent such interconnection, the costs were far higher than the telephone companies' costs of providing such custom calling services on an integrated basis, and this may explain why alternatives have not arisen.<sup>15/</sup>

Since other voice messaging services were never provided the BOC network features they needed to offer mass market voice messaging services, the dearth of such services is not the fault of structural separation, but, rather, must be attributed to the BOCs' failure to provide nondiscriminatory access to reasonably priced network features needed to provide enhanced services.

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<sup>15/</sup> Amendment of Section 64.702 of the Commission's Rules and Regulations, CC Docket No. 85-229, Phase I, 50 Fed. Reg. 33581, 33582 n.8 (Aug. 20, 1985) (Notice of Proposed Rulemaking) (emphasis added).

In fact, as was vividly demonstrated by the MemoryCall case<sup>16/</sup> and other evidence submitted in the Computer III Remand proceeding, as well as in the initial comments and other filings in this proceeding, voice messaging providers have not been provided such nondiscriminatory, reasonably priced access. The statement of a voice messaging provider attached to a report by Hatfield Associates being filed today (Hatfield Reply) illustrates the problems faced by such providers.<sup>17/</sup> All of these abuses are discussed in Part II, infra.

There is therefore no logical basis to conclude that the BOCs' unseparated provision of voice messaging services has produced the benefit of satisfying a previously unserved market. That market, to the extent it was unserved, was not being served because of the BOCs' denial of reasonably priced access to their networks. The BOCs' dominance of the residential voice messaging market thus is not an example of the benefits of unseparated BOC enhanced services, but, rather, a stark illustration of the dangers of discriminatory access that are exacerbated by the joint provision of services.

The BOCs also argue that their low penetration rates in

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<sup>16/</sup> In the Matter of the Commission's Investigation into Southern Bell Telephone and Telegraph Company's Provision of MemoryCall Service, Docket No. 4000-U (Ga. PSC, June 4, 1991).

<sup>17/</sup> Hatfield Associates, Inc., The Benefits of Structural Separation: Reply (May 19, 1995), Attachment.

enhanced services other than mass market voice messaging demonstrate that their participation in the enhanced services market on an unseparated basis presents no risk of anticompetitive conduct.<sup>18/</sup> The pattern of BOC penetration, however, demonstrates just the reverse -- namely, that the BOCs have not accomplished much in the enhanced services market other than in mass market voice messaging, where there have been the most BOC abuses, and in that market, they have attained overwhelming dominance.<sup>19/</sup> That pattern shows that BOC provision of unseparated enhanced services has not produced significant public benefits, but it has allowed for tremendous abuses.

Accordingly, continuation of the structural separation requirement would not lead to foregone benefits, as the BOCs argue. In those areas where they remain insignificant, structural integration has clearly made no difference, and in mass market voice messaging, the way to generate significant public benefits is to require the BOCs to do what they should have done in the wake of the Custom Calling Denial Order -- provide reasonably priced network access to voice messaging providers, as well as to all ESPs. The elimination of structural separation thus drops out as a causative public benefits factor

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<sup>18/</sup> BellSouth Comments at 56-57 & n.69; Southwestern Bell Comments at 7-10, 39; NYNEX Comments at 22-23; US West Comments at 5, 11-13; Ameritech Comments at 8-9.

<sup>19/</sup> See n. 10, supra.

in any enhanced service market.<sup>20/</sup>

It is also ludicrous for the BOCs to claim that only they have been subject to structural separation, while the rest of the industry offers services on a joint basis.<sup>21/</sup> Southwestern Bell, for example, expresses considerable envy toward competitors, such as MCI, which offer a variety of services on an integrated basis, and argues that eliminating the structural separation requirement is the least the Commission can do to reduce the BOCs' tremendous disadvantage in this regard.<sup>22/</sup> In fact, the reality is just the opposite. The rest of the enhanced service industry is entirely separated from the BOCs' network operations. If mere structural separation is a "handicap," as Ameritech claims,<sup>23/</sup> ESPs are far more handicapped by complete separation from the BOCs' networks. That the rest of the industry, other than mass market voice mail,

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<sup>20/</sup> As MCI pointed out in its initial comments, the Notice properly takes the view that in order to show that "a" causes "b", it must be shown that only "a" can cause "b"; or "non-a" causes "non-b". MCI Comments at 12-13, n.29. MCI cited the Notice, at ¶ 39, which stated that parties should "identify the benefits" of structural separation "and articulate why these benefits cannot be achieved under a regime of nonstructural safeguards," under structural integration. The same is true for the purported benefits of structural integration. If the very same public benefits (e.g., mass market voice messaging services) could have resulted whether or not structural separation was eliminated, the growth in mass market voice messaging services cannot be considered a public benefit that can be attributed to the elimination of structural separation.

<sup>21/</sup> See, e.g., Bell Atlantic Comments at 18-19.

<sup>22/</sup> Southwestern Bell Comments at 35-41.

<sup>23/</sup> Ameritech Comments at 2.

has thrived despite its complete separation from the BOCs' local networks is the most vivid illustration of the lack of public need for, and lack of public benefits from, joint BOC basic and enhanced services.

Pacific Bell uses Centrex as its illustration of the benefits of joint BOC services. Pacific Bell argues that it needs to be able to sell Centrex and voice mail together in order to compete with entities such as MCI, which "will integrate its Network Voice Mail with the customer's private branch exchange (PBX) or Centrex, if desired, or function as a traditional service bureau."<sup>24/</sup> That example, however, demonstrates the opposite of Pacific Bell's point, since MCI is simply selling its voice mail service to a customer who already has PBX or Centrex service provided by another entity -- almost always Pacific Bell -- just as a BOC's enhanced service subsidiary could provide voice mail service to a customer that already had PBX or Centrex service provided by the BOC's network services subsidiary.

It is especially ironic that Pacific Bell mentions its Centrex service in this regard, since the California Public Utilities Commission (CPUC) just issued an injunction requiring Pacific Bell to cease and desist from its practice of refusing to allow its Centrex customers to program their Centrex systems to

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<sup>24/</sup> Pacific Bell Comments at 75-76, citing research paper.

route intraLATA toll calls automatically to competing carriers.<sup>25/</sup> The CPUC found that this practice was likely to cause irreparable competitive injury to other carriers offering intraLATA toll service and that Pacific Bell "is attempting to maintain a monopoly in the intraLATA toll market by... such refusal."<sup>26/</sup> The CPUC explained that a Centrex customer that cannot route its toll calls to MCI or another competitive carrier is more likely to enter into a term agreement with Pacific Bell for intraLATA service and thus less likely to use competitors' services. Under those conditions, other carriers cannot compete for intraLATA toll business.<sup>27/</sup>

A fortiori, Centrex customers whose use of MCI's toll service is obstructed by such practices would certainly be less likely to use MCI's voice messaging service, leaving that segment of the voice messaging market entirely in Pacific Bell's grip. Joint provision of Pacific Bell's Centrex and voice mail services thus extends the effects of Pacific Bell's anticompetitive abuse in the Centrex market to the voice mail market. It is indeed fitting that Pacific Bell pointed to the Centrex situation as its illustration of the "benefits" of structural integration, since the supposed efficiencies of structural integration are typically

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<sup>25/</sup> Opinion, MCI Telecommunications Corp. v. Pacific Bell, Case No. 94-12-032, Decision 95-05-020 (CPUC May 11, 1995).

<sup>26/</sup> Id., slip op. at 61

<sup>27/</sup> Id.

monopoly leveraging and cross subsidization in disguise.<sup>28/</sup>

Finally, if the BOCs' goal is "one-stop shopping," there is nothing to prevent that under structural separation. Just as, in Southwestern Bell's example, MCI resells others' services in a package with its own enhanced services,<sup>29/</sup> a BOC enhanced services subsidiary could resell the BOC network service subsidiary's tariffed offerings together with its own enhanced services and could market such basic and enhanced services as a package. Assuming that the same tariffed services were equally available to all comers on the same terms, including unrestricted resale, and all of the nonstructural safeguards also applied, such joint marketing by the BOC enhanced services subsidiary would meet the BOCs' legitimate efficiency goals without leveraging the BOC network monopoly. Such an arrangement would also help further the Commission's resale policies by inducing the BOCs to maximize opportunities for their enhanced service subsidiaries by pressing state commissions for unrestricted resale of all regulated services. If such a resale arrangement is not satisfactory to the BOCs, their stated goal of efficiency is really a Trojan Horse for monopoly leveraging.

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<sup>28/</sup> See Hatfield Reply at 2-5; CompuServe Comments at 24-25.

<sup>29/</sup> Southwestern Bell Comments at 36.

B. The BOCs' Showings of the Supposed Costs of Structural Separation Are Irrelevant and Inadequate

In a repetition of the arguments from the Computer III Remand proceeding, the BOCs, supported by various outside consultants' reports, offer estimates of the costs to the BOCs of structural separation as another benefit of structural integration that would be foregone under structural separation. (These costs are in addition to the supposed consumer welfare loss resulting from the delay in introducing voice mail.)

A large part of the costs to the BOCs are the one-time costs of moving their enhanced services to separate subsidiaries. As MCI and CompuServe Incorporated explained in their initial comments, however, the one-time costs of moving to structural separation are irrelevant in any proper cost-benefit policy analysis of the structural separation issue. Since California III returned the industry to the Computer II structural separation regime,<sup>30/</sup> the BOCs already would have set up separate subsidiaries for their enhanced services were it not for the interim waiver granted pending the outcome of this proceeding.<sup>31/</sup> The BOCs understood that, in being granted a waiver of the status

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<sup>30/</sup> Amendment of Section 64.702 of the Commission's Rules and Regulations, 77 FCC 2d 384 (1980), mod. on reconsideration, 84 FCC 2d 50 (1981), mod. on further reconsideration, 88 FCC 2d 512 (1981), aff'd sub nom. Computer and Communications Industry Ass'n. v. FCC, 693 F.2d 198 (D.C. Cir. 1982), cert. denied, 461 U.S. 938 (1983).

<sup>31/</sup> Bell Operating Companies' Joint Petition for Waiver of Computer II Rules, DA 95-36 (CCB released January 11, 1995).



quo -- structural separation -- they had no standing to object to a termination of the waiver returning them to the policy status quo. The costs of moving to the status quo, albeit temporarily waived, thus cannot be considered in determining whether the status quo should be changed.<sup>32/</sup>

Aside from the irrelevance of the one-time costs of setting up enhanced service subsidiaries, the BOCs' demonstrations of the costs of structural separation are superficial and unproven. The Hatfield Reply discusses the analytical flaws of the four BOC consultants' submissions on this issue. As the Hatfield Reply explains, the supposed economies of scope arising from structural integration should be viewed with great skepticism and ought to be available without service integration. Such economies are doubtful partly because jointly used facilities under structural integration are often designed for enhanced service needs and are therefore costlier than facilities needed only for regulated services. The Hatfield Reply goes on to explain why the BOCs' low penetration rates into most enhanced service markets does not necessarily mean that their participation on an unseparated basis is without risk. The monopoly BOCs' low market share in most enhanced services merely demonstrates their ineptness in competitive services. The Hatfield Reply answers the BOCs' claims as to the benefits of one-stop shopping by pointing out that the BOCs can have the benefits of one-stop shopping under

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<sup>32/</sup> See MCI Comments at 10-12; CompuServe Comments at 25-26.

structural separation by simply having a BOC's enhanced service subsidiary resell the BOC regulated subsidiary's services.

The Hatfield Reply also rebuts the Hausman/Tardiff estimate of consumer welfare losses resulting from the alleged delay in introducing voice mail, explaining that such delay cannot necessarily be attributed to structural separation. It also rebuts the estimates of increased costs to the BOCs resulting from structural separation. Those costs are largely due to the BOCs' failure to meet their original ONA promises and to excess capacity in the BOCs' regulated operations.

The BOCs' comments are equally unpersuasive. BellSouth estimates that its unit sales costs would increase by 209%, advertising costs would increase by 300%, customer service costs would increase by 40%, and facilities costs would increase by 105%, for an overall weighted increase in costs of 176%.<sup>33/</sup> Other than discussing generally why such costs would increase under structural separation, BellSouth makes no effort to support these figures. Bell Atlantic and NYNEX make slightly more of an effort to support their estimates, but there is still no systematic analysis in those filings showing the derivation of their figures. Except for the one-time costs of moving its voice mail services, Pacific Bell provides neither a dollar figure nor an estimated percentage cost increase resulting from structural

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<sup>33/</sup> BellSouth Comments at 60-64.

separation.<sup>34/</sup> These comments and supporting materials also suffer from the same flaws as the BOC consultants' filings, discussed in the Hatfield Reply.

Moreover, some of the alleged increased costs and inefficiencies do not seem realistic. For example, some of the BOCs mention the need for additional marketing and service personnel to staff separate subsidiaries.<sup>35/</sup> Since the current personnel handle both basic and enhanced services, however, the splitting off of the enhanced services functions should not require additional personnel, but rather, a division of the current personnel. Additional personnel would only be needed if a carrier were overstaffing its basic service operations or planning to do so.

Some of the BOCs also mention increased advertising costs resulting from the need for separate advertising for basic and enhanced services.<sup>36/</sup> There is no need, however, to advertise monopoly basic services, including the complementary network services (CNSs) associated with enhanced services. CNSs will be needed by anyone using related enhanced services, whether the

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<sup>34/</sup> Pacific Bell Comments at 71-76.

<sup>35/</sup> See, e.g., BellSouth Comments at 60-62; NYNEX Comments at 24; Pacific Bell Comments at 72; Bell Atlantic Comments at 18 & Declaration of Robert N. Garner at ¶ 7.

<sup>36/</sup> BellSouth Comments at 61; Pacific Bell Comments at 72; Declaration of Robert N. Garner at ¶ 7 attached to Bell Atlantic Comments.

latter are offered by the BOC's separate affiliate or by an ESP. When the customer orders the enhanced service, he or she will be told to order the necessary CNSs from the BOC. No advertising for the CNSs will be necessary. It also seems doubtful that the separated provision of basic and enhanced services will create significant customer confusion as alleged by the BOCs,<sup>37/</sup> especially given the separate subsidiaries the BOCs already use voluntarily. None of the Computer II structural separation rules requires a BOC to keep the corporate connection between its basic and enhanced service subsidiaries a complete secret from the public.

Southwestern Bell also suggests that structural separation would negatively influence BOC investment decisions by causing the BOCs to disregard future enhanced service revenue in making such decisions.<sup>38/</sup> That seems somewhat far-fetched. A separate enhanced services subsidiary is hardly "out-of-sight, out-of-mind" to a competent CFO.<sup>39/</sup>

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<sup>37/</sup> See, e.g., BellSouth Comments at 59, 61, 63.

<sup>38/</sup> Southwestern Bell Comments at 33.

<sup>39/</sup> An even more far-fetched problem invented by Southwestern Bell, at 33-35, is its notion that customers will not get the benefit of advanced technologies, such as CCS using the SS7 protocol, if structural separation is reimposed, since many applications of those technologies are enhanced but could not be provided efficiently through a separate subsidiary. Technologies are not inherently basic or enhanced, however. There is nothing about the nature of the technology used that makes a particular application enhanced. Southwestern has not explained why the basic/enhanced determination might have to be made "on a message-  
(continued...)"

The BOC and Hausman/Tardiff cost estimates are also invalidated by their reliance on the BOCs' own inflated costs and aversion to physical collocation. The BOCs are still burdened by bloated cost structures developed under rate-of-return regulation. Price cap regulation, because of the easily-met productivity factor, has not significantly affected those costs. There is no reason to expect that BOC separate subsidiaries would be immune from the BOCs' bloated cost structures. Similarly, the BOCs' aversion to collocation inflates their cost estimates because it requires them to house their separated enhanced services in separate buildings, with all of the extra power, maintenance, trunking and other costs attached thereto. Their estimates of the costs of structural separation thus are partly a self-inflicted burden, which should not be permitted to "tilt" the public policy cost-benefit analysis to be conducted in this proceeding. That the BOCs' cost estimates, even if "accurate," reflect unnecessarily excessive costs is confirmed by the existence of so many ESPs, all of which are completely separated from the BOCs' networks, but which are also not burdened by the BOCs' monopoly rate-of-return cost structures.

It is also unclear whether these estimated cost increases, even if they were accurate, would make any difference in terms of

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<sup>39/</sup>(...continued)  
by-message basis," *id.* at 34, anymore than it is now in making the decision as to whether or not to tariff the service. See also, Part I(C), infra.

the rates charged to consumers. Information as to the costs and earnings of the BOCs' enhanced services is not available, but there is no reason to believe that they do not enjoy tremendous profit margins on their enhanced services.<sup>40/</sup> If that is the case, cost increases of 100%-200% might not make any difference in terms of the prices that the BOCs are able to charge. Thus, it is quite possible that the BOCs' enhanced services could still be made available to the public at the same rates. The only difference would be profit margins for the BOCs that were less outrageous but still sufficiently attractive to justify BOC participation in the same enhanced services.

In any event, the BOCs have not provided any information on the total costs and profit margins in their enhanced services so as to demonstrate the relative impact of their estimates of cost increases. Instead, they affect a lack of certainty as to such data -- data that they surely possess. For example, BellSouth states simply that "[i]t is unlikely that BellSouth MemoryCall could absorb the total cost impact of transitioning to a separate subsidiary without passing some of those costs on to consumers."<sup>41/</sup> Similarly, NYNEX states that under structural separation, it is "likely" that its voice messaging service would

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<sup>40/</sup> Because the BOC network features made available to ESPs are so overpriced, however (see ITAA Comments at 27-29), the BOCs can still undersell their ESP competition while making tremendous profits.

<sup>41/</sup> BellSouth Comments at 64.

have been limited to large businesses or to the largest urban areas.<sup>42/</sup> Pacific Bell says nothing about the impact of the increased costs on the viability of its enhanced services.

The BOCs ought to know precisely whether any of the supposed cost increases would have to be passed on, how much and the impact of such cost increases on their enhanced services. That these BOCs are unwilling to present such an analysis, with supporting data, speaks volumes as to the credibility of their estimates.<sup>43/</sup> It must be concluded that the BOCs have not made a credible showing of increased costs resulting from structural separation that will have a significant impact on their enhanced service offerings.

C. The Regulatory Classification of Protocol Processing  
Should Not Be Changed

Related to the BOCs' efficiency arguments is Bell Atlantic's proposal to modify the enhanced services definition to omit protocol processing, thus making protocol processing a basic service. Bell Atlantic argues that changes in technology have made the classification of protocol processing as enhanced unworkable. Today, protocol processing is necessary to connect

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<sup>42/</sup> Affidavit of William B. Neil, Jr., at 6, attached to NYNEX Comments.

<sup>43/</sup> Bell Atlantic estimates that structural separation would raise the price of its voice messaging service about 25%, but provides no data to support that figure. See Declaration of Robert N. Garner at ¶ 7, attached to Bell Atlantic Comments.

"disparate terminals" to a variety of interconnected networks, typically requiring protocol conversion at each interconnection point, and the most efficient location for the conversion is in network, rather than at the terminal, according to Bell Atlantic. Bell Atlantic concludes that it would be more efficient to treat protocol processing as a basic service so as to avoid having to interrupt otherwise seamless interconnected networks with cumbersome regulatory requirements.<sup>44/</sup> US West raises similar efficiency arguments against the imposition of structural separation requirements on BOC protocol processing services, but does not directly challenge the classification of protocol processing as enhanced.<sup>45/</sup>

None of the developments described by Bell Atlantic provides any justification for the radical, retrogressive step Bell Atlantic proposes. Regulation of protocol conversion as a Title II common carrier service, first of all, would constitute a giant step backward toward reregulation, contrary to the deregulatory trend of the past 20 years. Thousands of entities that have been unregulated would be swept within the scope of Title II, threatening the vigorous competition that has developed in the value added network (VAN) industry as the result of the unregulated status of protocol processing. Regulation of protocol processing as a basic service would force all of those

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<sup>44/</sup> Bell Atlantic Comments at 33-36 and Attachment D.

<sup>45/</sup> US West Comments at 6-7.



entities to file tariffs for their VAN services, burdening the industry and the Commission and stifling competition.

Moreover, Bell Atlantic has failed to demonstrate any justification for such a radical, burdensome change. Bell Atlantic concedes that the problem it has identified is relatively short term, caused by the transition to a likely industry-wide uniform ATM standard. Once such a uniform internetwork standard is achieved, there will be relatively little need for internetwork protocol conversions.<sup>46/</sup> It makes no sense to promulgate a permanent regulatory change to meet what is, at most, a transitional problem, especially given the upheaval in the enhanced services industry that such a change would cause.

Furthermore, it is not at all clear why a widespread need for internetwork protocol conversions should raise any issue at all as to the regulatory status of protocol processing. Where a customer needs to connect disparate terminals and/or local or wide area networks, it can be provided an enhanced application that includes optional protocol conversion. That the customer might not need protocol conversion for a particular transmission is irrelevant; the availability of protocol conversion makes the application enhanced. A BOC would provide such an application out of its enhanced services subsidiary.

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<sup>46/</sup> Bell Atlantic Comments at 35.